CalPERS

CalPERS Responds to the Howard Jarvis Taxpayers Association Report of January 2007

The Howard Jarvis Report fails to provide the public with a complete, up to date and accurate assessment of the financial soundness of public pension systems in California, and particularly, the financial soundness of the California Public Employees' Retirement System (CalPERS).

Contrary to the findings of the Jarvis report issued today, CalPERS funding is stronger than ever before, with record breaking asset growth, more stable employer rate contribution requirements, and a funded status that is high.

The report's conclusions hinge on a "snapshot" of activity artificially constrained to a period of market downturn and early stages of its recovery. CalPERS is disappointed that a more objective report was not provided.

CalPERS picture of health includes the following:

- **Since the market downturn period contained in the Jarvis Association report, CalPERS assets have grown by $100 billion to a record $225 billion in assets today and doubled in the past 10 years.**
- **The funded status of CalPERS – which had dipped to 81 percent during the market downturn – has risen back up to nearly 90 percent fully funded this year.**
- **A revised actuarial smoothing policy that keeps annual employer contributions stable has been adopted, providing local governments with realistic budget planning from year to year.**

Below are specific observations about the Jarvis Report:

Flawed Methodology Used

- Flawed methodology: the relatively brief window for assessing the overall financial status of public funds starts at the stock market peak in the late 1990s. It focuses on the years of declining stock returns to show a huge decline in funded status. Those years were an anomaly and do not represent an accurate long-term picture of CalPERS and other public pension funds.

- The study begins its analysis of CalPERS unfunded liability when the System was <u>most</u> funded to its <u>least</u> funded point after a three-year downturn in the stock market – the worst since the Great Depression. The bear market significantly reduced funding levels from 130 percent in many cases to about 85 percent funding in about three years. *The more complete record shows an <u>increase</u> in funded status from 81 percent on June 30, 2003 to more than 90 percent. Moreover, tracking from the beginning of the CalPERS program, or even for a 20-year period, shows <u>steady growth</u> and <u>substantial continuity in security</u>.*

Selective figures & spurious comparisons

- The comparison of public employee benefit payments to State tax revenues is misleading because the cash from benefit payments nearly exclusively comes from income from investments – not from tax dollars. For example, Item 2 of Section 1 refers to public employee retirement benefits totaling $20 billion while total state income tax revenues the same year totaled $38 billion. Pension benefits do not come for income tax revenues. Pension benefits come from a pre-funded trust fund. *A fair comparison would match total income of the pension fund to the total payments each year. The income should include investment returns that comprise most the pension fund's revenue gains.*

- The study unfairly compares benefit payments of 1997-98 to payments of 2003-04 to show an increase – without identifying that the source of the increase is due to additional growth in the numbers of persons who are retiring, and that funds are already set aside for distribution.

- The study fails to state that State contribution increases represent a small part of the general fund budget – roughly about 0.24 percent of the proposed general fund budget of $100 billion in the fiscal year of the highest spike in contributions.

- The study unfairly compares the average annual salary of CalPERS members in California to average California per capita personal income. A fairer comparison would be to workers in similar job categories.

- Regarding costs to employers, the study stretches the facts and mixes apples and oranges (See Table 1-6). The appropriate focus is the contribution rates into the System as percent of payroll. The study's own chart shows an overall decline of employer rates. Only counties and special districts showed an increase.

- The report often uses extreme examples and comparisons that are not common or normal. (For example, Item 7 of Section 1 of the Executive Summary asserts that "general" employees in many systems can retire at age 55 after 16 years and receive over 40 percent of their salaries. It refers to the rare 2.7 at 55 retirement formula, which very few cities have. State employees and most local government employees have a much lower retirement formula – 2 percent at 55. School teachers in CalSTRS have a 2 percent at 60 formula.

- The report is not independently verifiable due the lack of proper footnoting. It gives only general references for data.

- Many public sector jobs aren't comparable to those in the private sector; public sector jobs that are comparable to those in the private sector receive less total compensation.

- It is a gross overstatement to say that employee retirement contributions are often paid partly or fully by employers. In a vast majority of cases, employees pay their own contributions.

Increasing benefits: government largesse or demographics?

- Increased benefits are the natural result of an aging population. Employers have been paying in for years for employees hired in the 1960s, '70s, and '80s, when California experienced a great population increase.

- The suggestion of "lavish" public pensions differs from fact. The average CalPERS benefit is $1,876 per month (as of June 30, 2006). By comparison, a full-time worker paid $11 per hour would gross $1,903.

The Up-to-Date Review of CalPERS includes the following facts:

- The CalPERS fund has grown by almost $100 billion since recovering from the market downturn, now totaling more than $225 billion.
- Investments last fiscal year earned 13 percent, well above the assumed rate of return of 7.75 percent.
- CalPERS funded ratio is nearly 90 percent.

- Actuarial smoothing policies provide employers with more predictable contribution schedules from year to year.
- FY 2006-7 state employer rate increase of $236 million is a small additional expense that did not materially affect its financial condition, and represented 0.24 percent of the general fund budget of $100 billion, less than 2 percent of the state's payroll of $13.8 billion, and was less than 5 percent of the higher than expected tax revenues.
- Several factors have offset asset gains, including higher than projected retirements, delayed salary increases that took effect, and fewer than expected retiree deaths.
- Pre-funded pension systems continue to be a cost-effective method for financing pensions, and minimizing taxpayer contributions.
- The vast majority of CalPERS retirement benefits go back into the California economy, since recipients live in the state.